

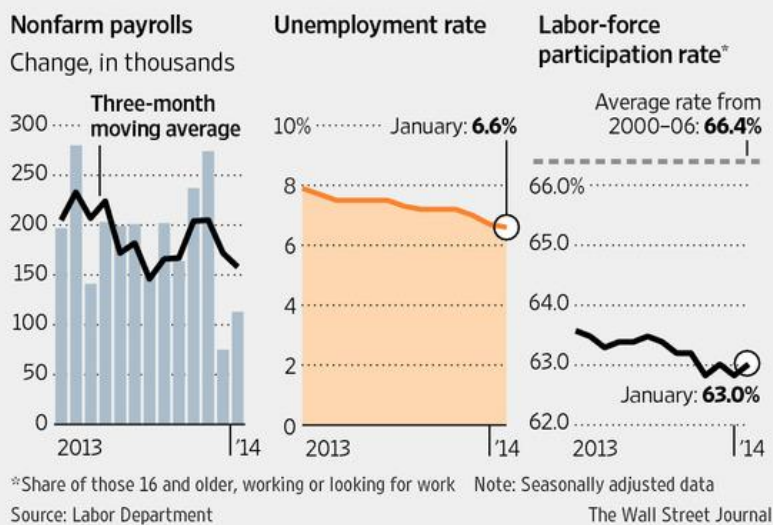
Weekly Report – February 11, 2014

The Debt Ceiling

- Treasury Secretary Jacob Lew reiterated his position that the Treasury will not be able to utilize extraordinary measures beyond February 27, 2014.
- The Treasury officially hit the debt limit on February 7, with debt outstanding of \$17.258 trillion.
- Different options have been discussed to add to any increase in the debt limit. There may be a bill on the House floor this week.
- The Bipartisan Policy Center had projected the X date, or day when Treasury will have exhausted its extraordinary measures and not have sufficient cash on hand to pay all obligations, as between February 28 and March 25. Specifically, the X date was estimated to have occurred by March 14.



Wintry Mix | January's jobs report



The January Jobs Report

- The January Jobs Report released on Friday, January 7, highlighted a weak job market with only 113,000 jobs added this month, and 75,000 last month.
- The December and January reports represent the slowest two-month pace for job creation in three years.

Budget Schedule Ahead

- The House Budget Committee has scheduled a hearing with OMB Director Sylvia Burwell on March 5 to review the President's budget.
- The House is expected to take up its budget proposal in early April.

RSC 2015 Budget – Reviewing Budget Proposals

- The Budget and Spending Task Force has commenced analysis of ideas for inclusion in the RSC FY2015 Budget. To share policy ideas and participate in the budget crafting process please contact either Matt Dickerson with RSC at matthew.dickerson@mail.house.gov, or Nick Myers in Congressman Woodall's Office at x: 5-4272 or nick.myers@mail.house.gov.

Jay Pelosky: Ominous Signs for the Global Recovery – *U.S. growth may be ready to cool, Europe faces a serious deflation risk, and emerging markets are in disarray.*

As the feel-good talk emanating from the World Economic Forum gathering at Davos last month fades and equity investors contemplate the possibility of a major market correction, a combination of factors suggests that something ominous may be afoot. Taken together, these three factors—simultaneous liquidity withdrawal by the Federal Reserve and China, a U.S. stock market on a knife's edge, and emerging markets in disarray—indicate that the global economy could be in danger of snatching defeat from the jaws of victory.

Some observers continue to predict a synchronized global recovery in 2014. The U.S. economy is accelerating, the story goes, Europe has bottomed and will return to growth, while Japan has turned the corner on deflation. China is stable at 7% GDP growth, and the rest of the emerging world is stronger than in prior crises, such as the one in 1998. The counterargument suggests that the U.S. economy is ready to cool; that Europe faces a serious risk of deflation; and that Japan needs to do much more to ensure that growth and gradual inflation are entrenched. China is trying to deflate a credit bubble while the remainder of the emerging markets are divided among the mismanaged, the overly indebted and the unbalanced.



Chad Crowe

The current geo-economic framework may help to determine which of these visions is likely to play out. This framework suggests that the world economy has yet to find and implement new growth models to replace those broken in the past decade: the U.S. consumer engine, European vendor-financed growth and the emerging markets' export-driven model. Three additional factors are critical to understanding the global economic outlook. First, the adjustment to the new post-crisis economics has been buffered by the Fed's unprecedented "quantitative easing" programs in the U.S. and record credit expansion in China. Now these two wellsprings of post-crisis liquidity and economic activity are drying up at the same time, with no growth-model replacement or policy at hand. This is a worrisome development, given the underlying realities of inadequate global demand and very low inflation.

Second, the U.S. stock market, up more than 30% in 2013, teeters between a growth scare on one side and a worst-case scenario of the Fed tapering its monthly QE bond purchases in a weakening economy on the other. The growth scare: better U.S. economic data leading to investor fears that the Fed is behind the curve, resulting in sharply higher interest rates that in turn spur a major stock selloff. The worst-case scenario—so-called because if the Fed tapers and growth disappoints, there is very little to sustain the stock market at current levels—is coming into view as Janet Yellen settles in as the new Fed chairman. A reading of Fed history suggests that its new leaders are tested by markets within the first six months. Ms. Yellen may well have to consider pausing or even reversing the taper process in her first few meetings.

Third, in regard to emerging markets, a Mike Tyson quote comes to mind: "Everybody has a plan until they get punched in the mouth." Emerging economies from South America to Asia to Africa have been pummeled lately, and they're trying to figure out what to do. Their actions could push the world economy to a tipping point where hopes of a synchronized global recovery evaporate. Given that emerging markets generate more than 50% of global GDP on a purchasing-power parity basis, what's happening in those countries should not be underestimated or dismissed. The trifecta of emerging-market miseries goes like this: The mismanaged: Venezuela and Argentina have devalued. The overly indebted: China and many of its Asian neighbors face very tough conditions created by the consumer-debt bubble. China is just beginning to try to stabilize a credit system that is opaque in the extreme. One example should suffice: The over \$1 trillion "local trust" lending market, which itself has more than \$600 billion coming due this year. The unbalanced: Various large nations, including Indonesia, Brazil, Turkey and South Africa, have large current-account deficits and thus depend on external financing. For most of these unbalanced countries, 2014 is also an election year, which sharply limits policy flexibility.

For emerging markets, the combination of risk-averse leaders, large, immediate external-financing needs and poor market conditions suggests only a few, mostly unattractive, policy options. They range from devaluing currencies to imposing capital controls to prevent capital flight (which doesn't address external capital-raising needs) or raising interest rates high enough that foreign capital considers itself paid for the risk. Because large currency devaluations are often political career-enders, raising interest rates tends to become the first choice. The problem is that doing so crushes local demand—the very growth model that emerging economies have been working toward. Consumer demand in these economies is also what Western companies, investors and policy makers are attracted to. All this means that troubled emerging markets are likely to be in the headlines throughout the year. Moreover, emerging-market volatility and slower growth means that oil prices are at risk of a significant decline. Meanwhile, emerging-market devaluations and financial upheaval will increase the demand for gold. As a result, the "synchronized global recovery" may be dead on arrival, replaced by the specter of deflation.

Let's hope 2014 doesn't punch like Mike Tyson. But if the Fed tapers and global markets and growth continue to slide, Ms. Yellen and her fellow policy makers at the European Central Bank and [Bank of Japan](#) will have to do much more to avert another lost year for the global economy.

Mr. Pelosky is principal of J2Z Advisory LLC, a global asset-allocation and portfolio-strategy consultancy.